THE AFTER EFFECTS OF FREE COINAGE OF SILVER.

THE presidential election now pending has taken the shape of a referendum on the question of the free coinage of silver. Party divisions are broken down, and the personality of candidates counts for little. Those parts of the several party platforms that do not touch the monetary question are comparatively neglected. An economic issue that is little understood and is supremely important is submitted to a vote of the people. Never before has the principle of the referendum been put so searchingly to the test.

The actual decision of the question hinges mainly on the effects of the mere transition from one standard to another. What will happen during the operation of discarding gold and introducing silver? As regards this change in itself, the workman is virtually invited to relinquish a part of his wages and to get it again if he can. He is urged to vote that coins of small purchasing power be paid to him for his labor, and to take his chance of afterwards making his employers pay more of these coins. He is asked to let his savings-bank deposits, his insurance policies, *etc.*, be reduced in value. Debtors of every class, individuals, corporations and governments are urged to practice repudiation by euphemism. They are asked to pay their debts literally, dollar for dollar — that is, a cheap dollar for a good one. The price that the country would pay for such an advantage secured by debtors is already indicated by the loss of borrowing power that has followed the mere proposal. Coinage depreciation is credit annihilation. "Scale debts, and with them wages and savings. Repel the loans of capital that give employment. Destroy credit for the sake of 'booming' business." This is the demand made of the people.

Even in the presence of these critical and immediate issues, it is well to look beyond the mere transition from a gold stand-

ard to a silver one. Is silver capable of serving alone as good money for the United States? Assume that the transitional effects are past. Debtors have gained, creditors have lost, wage earners have suffered, business has passed through a convulsion and is in process of recovery. It is too much to assume that credit is restored; but let us say that enough of it survives to enable business to go on. Under the most favorable circumstances that can be assumed as possible, how will silver act as money in this country? What will be the permanent effect of using it?

In earlier articles I have called attention to the fact — obvious in itself, although the theoretical cause of it has not been duly studied — that a money which slowly and steadily gains in its purchasing power lowers the rate of interest on loans.[1] That money gains in purchasing power means that commodities in general lose in price. It is an all-around and uniform fall of prices. Of course different articles are affected by different influences, and change in value unequally. Independently of changes in a monetary system, some articles decline rapidly, some decline slowly, and some remain stable or even rise in price. The change in the monetary system is a further influence that acts upon them all. If metallic money is becoming scarce and costly to the extent of gaining in value one per cent a year, it follows that an article which would otherwise have fallen in price by five per cent will fall six per cent; an article that would have remained stable in price will lose one per cent; and an article that would have gained five per cent will gain only four. This fall in prices, if it be slow and steady, acts on the rate of interest as calculated in money. It is not best to repeat the argument by which this is proved, since the fact itself is scarcely in doubt. The theory that is behind the fact may be the subject of controversy; but any man who is able to transact business, and to borrow capital for the purpose, knows that he pays as interest, except in emergencies, only what he can afford to pay, and that he can afford to pay what the borrowed capital earns for him. The earnings come

[1] POLITICAL SCIENCE QUARTERLY, September, 1895 and June, 1896.

first in the form of goods. The shoe factory turns out more cases of shoes, and the blast furnace more tons of iron, in consequence of the new appliances that are procured through a loan of capital. The money that comes from the bank goes into machinery and raw materials; it creates finished goods, and these goods in themselves constitute the real interest on the borrowed capital.

The interest has to be paid in money, however, and so does the principal of the loan. If the machinery is shrinking in value, the price of it at the end of a year will not repay the principal. The borrower must provide for paying that as well as for paying interest, and he must keep some of the earnings of the capital for that purpose. In the illustrations given the manufacturers can not afford to pay to the bank, as interest, all the value of the shoes and of the iron that the new appliances create. They must keep some of the money that comes from the sale of these products to make good the declining value of the machinery and to enable them, in due time, to repay the money that they have borrowed. This is citing the obvious business fact that if a manufacturer has a plant that is declining in value, he can not pay the full price of its concrete products as interest on the loan that procured it for him. If a merchant has a stock of goods of which the average prices do not change, he can afford to pay one rate of interest; if his stock declines in value on his hands, he must pay a lower rate or trench on his own capital. In general he can get the loans at the lower rate; for if lenders try to exact more, their funds will in part remain unused. Capital, then, is loaned by the use of money. This money is converted into productive goods, which are then reconverted into money. The process looks like one by which money earns money, for by the intervention of goods more currency returns than was originally loaned. The amount of this returning money fixes the rate of interest on loans, and of course the amount is affected by changes in the prices of goods. Hence, falling prices mean reduced interest.

An inflation of the currency would raise prices. If it were to continue indefinitely and at a uniform rate, it would add to

the nominal rate of interest as paid for loans. Borrowers then would not gain by the rise in prices. On the other hand, a permanent and uniform contraction of the currency would reduce prices and would correspondingly reduce interest. This it has done during the past twenty years. Borrowers whose loans do not date from an earlier period have received the benefit of this reduction, and therefore have not suffered a clear loss through falling prices. If the production of gold, then, falls slightly behind the demand for it as the money of the world, — if there ensues what is equivalent to a slight and steady contraction of the currency of Europe and America, — it is safe to deny absolutely that results will follow that will burden borrowers, play into the hands of lenders, blight enterprise, *etc.* A reduction of the nominal rate of interest is all that will follow.

In stating these principles I have been aware of one large reservation with which they will be received. Steadiness in the movement of general prices caused by the appreciation of gold is essential to secure these results. A sudden rise in value of the monetary metal does what advocates of silver claim: it burdens borrowers, plays into lenders' hands and checks enterprise. Unsteadiness in the value of the monetary metal is a real blight on business. The two words that express what is most evil in currency are *unsteadiness* and *uncertainty*. Make the purchasing power of money rise and fall by movements that are irregular and incapable of calculation, and you give to the system the power to do in full measure the harm that has been dreaded as a consequence of the appreciation of gold.

Let us see how silver would act in this respect. The largest loss that can fall on a borrower comes to one who secures his loan when currency is rising in value and pays it off while currency is falling. It may be conceded that a serious hardship of this kind befell men who bought farms near the close of the Civil War and paid, or tried to pay, for them later. Such hardship would befall myriads of others if we should again enter on a policy of inflation and should afterwards abandon it. Permanent inflation, however, is impracticable. Even if we try to accomplish

it by the issuing of irredeemable paper, we must stop somewhere. Money must have some metallic basis; and though that basis were silver alone, it must give, in the long run, a contracting rather than an expanding currency. As I tried to show in one of the articles above referred to, it is the nature of any metallic money to become *relatively* scarce and costly as the world grows more populous and richer. Manufactured articles become relatively cheaper and metals become, by comparison, scarcer and dearer.

Use the present stock of silver in the world, then, as money with which to pay all current notes. By so doing you make one large addition to the volume of money of redemption now available. Thus you start an inflation that can not continue by the use of silver alone. In the hope of perpetuating the rise in prices, follow the silver with paper. By the action of the principle that we have stated, you will thus make the interest on loans higher. Every man who buys a farm while the inflation continues will pay a high rate of interest on an inflated purchase price. When you are forced to stop the paper issues, as in the end you must be, the price of the land will fall, and the rate of interest on new loans will fall also. The price of all produce will go down, and the farmer will struggle again, as in the years following the Civil War he had to struggle, with a fixed debt, a fixed rate of interest and falling prices. The early *post bellum* days will be reproduced. Entering on a policy of inflation is, therefore, inviting men again to suffer what those suffered whose hard experience is so frequently depicted in Populistic literature. Conceding all that is claimed as to the evil that comes from buying or mortgaging real property while the value of money is rising and paying the debt so incurred while that value is falling, it is evident that a policy of inflation would inflict exactly that evil on new victims, unless a method can be invented by which the inflation can continue forever. Rather than to inaugurate again a policy that would lead to such a state, or to anything remotely resembling it, it would be far cheaper for the government to seek out every surviving debtor whose land was mortgaged during the war period and pay his debt outright. On

no account should we put a myriad of new buyers of property through an experience parallel to that which some farmers now recall with so much of bitterness.

The greatest degree of evil, then, that changes in the purchasing power of money can produce comes when an experiment in inflation ultimately has to be discontinued. Remonetizing silver, however, would not permanently expand the currency; for silver is a metal, extracted from the earth like gold, and it can not in the long run increase in quantity as rapidly as the finished commodities turned out by machinery. In a decade silver would disappoint us, if we wished it to give us permanently rising prices. The original act of adding to the stock of gold now used as money the existing stock of silver would, indeed, be one grand act of inflation, causing an upward leap of prices; but after the prices of merchandise, land, *etc.*, had once adapted themselves to the new conditions, they would begin slowly to decline. It would be, in effect, inflation followed by contraction, with the evil consequences that such a transition involves. How serious those evils are many an American farmer knows by hard experience. Peculiarly wanton would be the public policy that should inflict them on a host of purchasers and debtors of the future.

Would not those evils cease if we should wait long enough, as those resulting from the paper issues of the war period are vanishing? As silver takes its turn in appreciating relatively to other commodities, shall we not, in the end, reach a state like that to which gold has brought us?

Silver will, certainly, gain in purchasing power, as gold is gaining. If the United States makes silver its sole money, the country will have an appreciating money. The evils that result from inflation succeeded by contraction are transitional, exhausting themselves in a half-century. It is hard for those on whom they fall; but the country recovers. Silver monometallism in America, if it were adhered to without the issuing of irredeemable paper that is foreshadowed, would end by giving us what we now have, a currency of increasing value as compared with merchandise. A country that hopes to

escape from that condition by substituting the one metal for the other will be disappointed. The last state of that land will, in fact, be worse than the first. Silver will grow costly, as does gold ; but it will appreciate less steadily than gold. The changes of its value will baffle calculation. By uncertain movements the value will go now upward, now downward, and again upward. The borrower will never know whether a fall in prices may not be impending which will make it hard to pay his debt ; nor will a lender ever know whether a rise in prices may not cheat him out of a part of the principal of his loan. The blight of uncertainty will, in short, be thrown on commercial dealings. If we adopt a currency made of silver, we shall have to plead guilty to much of the indictment now brought against appreciating money. Silver will do the deeds that are now imputed to gold. It will burden borrowers and check enterprise ; and it will do this by its unsteadiness.

It is alleged against gold that a large fraction of the annual product of it is used in the arts, and also that it is used by a circle of rich and undemocratic nations. In the current phraseology, the use of gold "ties us to plutocratic countries." These statements are made under the impression that they tell against the use of gold as money by the United States. What do these facts really signify?

That much gold goes into the arts means that there is a way of disposing of a surplus of the bullion with no disastrous change in its price. The market for it is very extensive and there is much elasticity in the demand for it, so that the production of it might vary from time to time without causing the price to change in any corresponding degree. The uses of gold can be indefinitely extended. This metal meets chiefly the desire for decoration. It is made into articles that serve as badges of caste, and ministers to a respectable and insatiable type of vanity which is universal in the human race. Give a man wheat till you glut his appetite and he will waste the surplus of it. A large crop of food produce thus gluts the desires of consumers, and causes the price for the whole supply to fall. It is the rigidity of the demand for farm products that

makes an overproduction of them disastrous. A great excess of gold, however, would have no such effect, for it would find uses. Elasticity is the striking fact about the demand for gold.

In this respect silver is more like wheat than is gold. The demand for it in the arts, as compared with that for gold, is smaller and, what is of decisive consequence, more rigid. Much more silver can be used, of course, but not without glutting the wants to which it now ministers and degrading it to lower uses. If a greatly increased output of this metal is used in the arts, it must be for purposes for which inferior metals are now employed. A forced consumption of any large surplus of it must greatly reduce its price. It is against the action of exactly this law of nature that the producers of silver are now contending. They wish it kept in the currency and, to that extent, out of the arts. In the inelastic natural market in which silver bullion now has to be sold, a relatively small surplus suffices to break down the price. This, to a producer, is reason enough for struggling to keep it in the currency. From the standpoint of the business community the producer's argument amounts to *citing that quality of silver which unfits it for use as money as the reason for so using it.*

The liability of silver to great variations in its bullion price, in consequence of changes in production, is the most serious objection to using it as the medium of exchange. Natural instability of value is the final objection to a monetary metal. Thus, the experiment of using platinum for coins encountered as its chief obstacle the fact that the demand for it in the arts is not elastic. In this respect silver is better than platinum, but it is worse than gold. It has the quality that makes the natural fluctuations of its value disproportionately large.

What is the meaning of the second accusation brought against gold? Is it well or ill that we should be attached to the richer nations?

So far as the material of our money is concerned, the fact means that in using gold we have what is used both as currency and as bullion by a circle of countries capable of taking a large quantity of any thing that they want. This contributes

in a decisive way to stability in the value of things there sold. It is important that the nations using gold should be large and rich; but it is also important that in commence they should be closely allied. We need a good market for surplus bullion; but we also need one that we can readily reach. Large and active mercantile dealings are a factor in steadying the value of currency. A quantity of gold thrown into the market of one nation divides itself among all countries with which that nation has active dealings.

Can South America and Asia furnish us outlets of this kind for silver? Can they pay for much of it? Are our dealings with them so intimate that an excess of precious metals in our own market can quickly reach them? For the single purpose of taking off our hands a surplus of a metal used for money, and so rendering the value of it stable, it must be confessed that "plutocracy" has its advantages. A rich market is better than a poor one; a large market is better than a small one; a market to which we are closely allied is better than one with which we have less intimate relations. In particular is an elastic market better than a rigid one; and this condition depends on the nature of the thing to be exported. It must cater to a want that is not easily glutted.

Each of these conditions of stable purchasing power is fulfilled by the metal gold: not one of them is fulfilled by silver. We are asked to discard the one and adopt the other. If we do it we shall have a money that is like gold in the fact that, in the long run, it will rise in value. It will be unlike gold in that it will rise unsteadily. Probably we shall, in the end, grow wise enough to return to the use of the steadier metal; but we shall have paid a high price for the wisdom.

JOHN B. CLARK.